

The Honorable Karen A. Overstreet
Chapter 11
Hearing Location: 700 Stewart St., Rm. 7206
Hearing Date: January 15, 2010
Hearing Time: 9:30 A.M.
Response Date: at time of hearing

**UNITED STATES BANKRUPTCY COURT
FOR THE WESTERN DISTRICT OF WASHINGTON
AT SEATTLE**

In re

QL2 SOFTWARE, INC.
316 Occidental Ave. S, Ste. 410
Seattle, WA 98104

Debtor.

Case No. 10-10209

DECLARATION OF SCOTT MILBURN IN
SUPPORT OF:

1. APPLICATION FOR ORDER TO PAY PRE-PETITION WAGES, BENEFITS AND WITHHOLDINGS
2. APPLICATION FOR ORDER AUTHORIZING DEBTOR TO MAINTAIN PRE-PETITION BANK ACCOUNTS AND CASH MANAGEMENT SYSTEM
3. APPLICATION FOR ORDER AUTHORIZING DEBTOR TO PAY CRITICAL VENDORS
4. APPLICATION FOR ORDER AUTHORIZING DEBTOR TO USE CASH COLLATERAL

I, Scott Milburn, make the following declaration under penalty of perjury under the laws of the State of Washington and the United States of America:

1. I am the Chief Operating Officer of QL2 Software, Inc., ("QL2"), which filed a voluntary petition under Chapter 11 (the "Bankruptcy Case") of the United States Bankruptcy Code

DECLARATION OF SCOTT MILBURN IN SUPP. OF APPLS. TO (i) PAY
PRE-PETITION WAGES, (ii) MAINTAIN BANK ACCTS, (iii) PAY
CRITICAL VENDORS and (iv) USE CASH COLLATERAL - 1
#736708 v1 / 40548-001

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1 (the "Code") in the United States Bankruptcy Court for the Western District of Washington at Seattle
2 ("Court") on January 11, 2010, at approximately 4:51 p.m. (the "Petition Date").

3 2. QL2 is a Washington corporation that provides its customers access to competitive
4 market intelligence data they need through an automated data gathering process.
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6 3. QL2 was founded in 2002. It has more than 260 customers in 40 countries, including
7 nine Fortune 50 companies. The QL2 client roster includes more than 100 airlines, three of the top five
8 global pharmaceuticals, and market leaders in retail, consumer products, and life sciences. Its revenue
9 has been increasing steadily - \$7.4M in 2007, \$11.1M in 2008, and \$11.9M in 2009. The company
10 projects 2010 revenue of \$16.1M. QL2 employs 167 people, including 43 in Seattle, seven in Atlanta,
11 three in London, and 114 in India.
12

13 4. QL2 was founded by Kelvin Chin and other individuals. After founding QL2, Chin was
14 sued individually for securities fraud from a prior, unrelated company he founded. The plaintiffs,
15 Tumelson Family Limited Partnership and individual Tumelson family members (hereafter collectively
16 "Tumelson"), obtained a judgment against Chin in 2005.
17

18 5. Chin has admitted under oath that he colluded with at least one other QL2 board
19 member to hide his interests in QL2 so Tumelson could not collect on this judgment against any of
20 Chin's equity in QL2 or any of his QL2 income. Chin sold 750,000 shares of his QL2 stock back to the
21 company, and formally resigned his position and any related wages from QL2.
22

23 6. Chin continued to be a senior executive with QL2, though he had no formal position or
24 formal salary. On March 25, 2008, QL2 received a letter from Tumelson's counsel threatening a
25 lawsuit against the company if Chin did not pay the outstanding judgment against him. On March 28,
26 2008, the QL2 board of directors terminated any further relationship of Kelvin Chin with QL2.
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1 7. Tumelson filed suit against QL2 and Chin on April 21, 2008, alleging fraudulent
2 conveyance regarding Chin's stock and other claims. Four days later the QL2 board engaged KPMG to
3 perform a forensic analysis of the operations of the company under Chin's leadership.
4

5 8. QL2 hired a new CEO, Russ Aldrich, in August 2008, and since then an entirely new
6 management team has been hired. No one who was in an executive position while Chin was involved
7 with QL2 remains with the company.

8 9. The Tumleson litigation continued throughout 2008 and 2009. QL2 incurred more than
9 \$1M in attorneys' and forensic accounting fees related to Chin's alleged malfeasance, the Tumelson
10 lawsuit, and other litigation that arose out of the actions of prior management.
11

12 10. In August 2009, QL2, the Tumelsons, and a former board member who has admitted to
13 being complicit with Chin, and who was also a named defendant in the suit, engaged in mediation. The
14 parties reached a settlement where QL2 agreed to pay the Tumelsons \$730,000 plus interest in a series
15 of payments beginning September 2009, with this obligation to be secured by QL2 accounts receivable.
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17 11. The terms of the final settlement agreement continued to be negotiated during
18 September and October as to terms beyond those to which they agreed at the mediation. As a result of
19 the ongoing negotiations, and in light of cash constraints, QL2 did not commence making payments to
20 the Tumelsons and took no steps to give the Tumelsons a security interest.
21

22 12. The Tumelsons filed a motion with the mediator to hold the mediation settlement
23 agreement enforceable and award an arbitration award (pursuant to that settlement agreement's terms)
24 against QL2. QL2 objected to the motion on the ground that there was no enforceable agreement since
25 the parties were still negotiating final material terms. The arbitrator entered an award in favor of the
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1 Tumelsons on October 2, 2009. The King County Superior Court entered a judgment on October 23,
2 2009, confirming the \$730,000 award and other terms of arbitration award against QL2.

3 13. QL2 and Tumelson thereafter negotiated a post-judgment final settlement agreement
4 dated **November 16, 2009**, under which QL2 was required to (i) provide the judgment creditor with the
5 security interest in its accounts receivable, (ii) issue 750,000 shares of QL2 stock to be held in escrow
6 as additional collateral, (iii) grant a security interest in QL2's patent as additional collateral, and (iv)
7 begin making payments on the obligation, including \$250,000 to be paid in November and December.
8 QL2 subsequently fulfilled its obligations under the final settlement agreement as to providing the
9 judgment creditor with the agreed to security. During the course of the negotiations of the final
10 settlement agreement, the Tumelsons garnished a QL2 bank account. That garnishment was released
11 when the final settlement agreement was executed.
12

13 14. Contemporaneous with the granting of the security interest in the accounts receivable,
14 QL2's prior secured creditor, Graham & Dunn PC, agreed to subordinate its security interest to
15 Tumelson.
16

17 15. In November and December 2009, QL2 paid the Tumelsons \$250,000 as part of the
18 payment plan under the November 16, 2009, settlement agreement.
19

20 16. QL2 has no accrued cash and no bank line of credit. Because of the nature of its
21 business, its cash flow is unsteady, causing short term challenges in meeting obligations. QL2 has
22 received indication from a lender that it will provide it with a line of credit for up to \$1,000,000 to be
23 secured with \$500,000 of its domestic accounts receivable and \$500,000 of its international accounts
24 receivable. That line would greatly ease the challenges faced by QL2 in managing its cash flow and
25 expenses.
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1 17. This lender requires a first priority secured position on QL2's accounts receivable and
2 patent. We approached Tumelson, who refused to subordinate their security interests in those assets
3 granted to them in November 2009. Accordingly, QL2 cannot obtain the line of credit in the absence of
4 either their agreement to subordinate (which is not forthcoming) or a termination of their security
5 interests. The security interests to Tumelson were granted on antecedent debts within 90 days of QL2's
6 bankruptcy filing and it is anticipated that QL2 will seek to have these security interests avoided in the
7 near future as part of this bankruptcy filing.
8

9 18. In the absence of a line of credit, and faced with the scheduled obligations to the
10 Tumelsons and antecedent debt to Graham & Dunn and several other historical, unsecured creditors, it
11 is unlikely that QL2 could survive the next two months without having to terminate all employees and
12 close the business entirely.
13

14 19. It is QL2's inability to obtain the bank line of credit that has forced it to proceed with the
15 Chapter 11 filing so it can obtain financing, smooth out its cash flow, and better manage the remaining
16 \$1.2M in non-operational debt that resulted directly from the admittedly fraudulent activities of Kelvin
17 Chin. Absent the currently scheduled payments on that debt, and with bank financing in place, QL2
18 projects EBITDA earnings in 2010 of between \$3 and \$4 million.
19

20 20. A prompt reorganization is required in order to maintain the value of the company, for
21 the benefit of its creditors, employees, and customers.
22

23 21. Wage Application. In an application filed concurrently with this Declaration, QL2 seeks
24 authority to pay the pre-petition payroll, benefits, and taxes, as well as pre-petition contract amounts to
25 its IT independent contractor, due as described in Exhibit A (summary of "Unpaid Payroll Expenses")
26 in an amount not to exceed **\$183,331.02**.
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21.1. It is essential that QL2 be allowed to meet its pre-petition payroll obligations, and its failure to do so would jeopardize its ability to provide prospective customer services. Accordingly, it is in the interest of QL2 and its creditors for QL2 to retain its employees post-petition.

21.2. The Unpaid Payroll Expenses are set forth in the attached **Exhibit A**, which include wages (contract amount for contractor), and various employee withholdings including 401(k) contributions, federal taxes, insurance and etc.

22. Cash Management Application. QL2 maintains bank accounts with Wells Fargo and Merrill Lynch (collectively the "Bank Accounts.") listed and described below.

Bank:	Description of Account:	Account No.:
Wells Fargo	Demand deposit	xxx6151
Wells Fargo	Business Market Rate	xxx8791
Merrill Lynch	Brokerage Money Account	xxx7J75

22.1. QL2's operations require, among other things, controlling and accounting for its revenues. The existing cash management system assures prompt receipt and allocation of funds and the generation of timely and accurate financial information necessary to manage QL2's operations. Failure to preserve the cash management system, particularly at a time when QL2 is subject to the operational dislocation attendant to its Chapter 11 filing, would disrupt QL2's ordinary and usual financial affairs and would impair its opportunity for reorganization.

22.2. Wells Fargo is an authorized bankruptcy depository. Further, Debtor believes that Wells Fargo and Merrill Lynch are, pursuant to the requirements of §345(b) of the Bankruptcy

Code, insured by a department, agency, or instrumentality of the United States, or backed by the full faith and credit of the United States.

22.3. QL2 proposes to continue to use the Bank Accounts as Debtor-in-Possession Accounts. In order to maintain a distinction between checks that were issues pre-petition, and those issued post-petition, QL2 will skip at least 100 sequential check numbers, and start the new sequence on with the next check number that it a multiple of 100.

22.4. QL2 has concurrently filed an application herein requesting entry of an order (the "Wage Order") authorizing QL2 to pay all prepetition wages, salaries, commissions, increases and related benefits, which were due, owing or accrued as of the Petition Date. Checks for payroll and related benefits will be written on the existing Checking Account.

23. Critical Vendor Application. QL2 maintains accounts with certain critical vendors listed and described below.

Vendor	Total	
Adhost Internet	8,770.00	Hosting service for QL2 servers running its online hosted service for customers. Absolutely essential for ongoing operations and subject to being turned off for non-payment, which would cripple its business.
Cascade Broadband, LLC	29,055.48	Internet access provider (bandwidth) to run its entire business. Absolutely essential for ongoing operations and subject to being turned off for non-payment, which would cripple its business.
Internap Network Services	25,555.61	Hosting service for QL2 servers running its online hosted service for customers. Absolutely essential for ongoing operations and subject to being turned off for non-payment, which would cripple its business.
First Insurance Funding Group	3,904.10	Monthly financing payment on its 11/09-11/10 commercial general liability insurance. Payment was due 1/1/10.
Travelers	1,210.00	Single premium for QL2 international commercial general liability insurance coverage for UK office. Payment was due 12/15/09. Policy could be terminated.
TOTAL	\$ 68,495.19	

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1 24. Cash Collateral Motion. I have reviewed a UCC search obtained by our counsel for QL2
2 dated January 11, 2010, which shows a number of equipment lease vendors with security interests in
3 personal property. It also shows blanket security interests in favor of (i) Graham & Dunn¹ and (ii) Kelly
4 Tumelson and Katie Taylor² (hereafter collectively the "Secured Creditors"), which I know to be
5 outstanding debts. The UCC search also shows a blanket security interest in favor of Sterling Bank
6 dating back to 2007 which I believe to have been filed in error as the Company has never had any
7 outstanding debt to Sterling Bank now or since 2007³.

8
9 24.1. QL2 requires the use of the cash collateral of the Secured Creditors, but I believe
10 that they will be adequately protected as required under applicable law. QL2 engaged Moss Adams to
11 appraise the value of its business and a report was issued in November 2008 showing the company's
12 value to be approximately \$9.6M.

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14 24.2. QL2 has debt outstanding to Graham & Dunn in the approximate amount of
15 \$579,000. QL2 has debt outstanding to Kelly Tumelson and Katie Taylor in the approximate amount
16 of \$520,000.

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18 24.3. While I am no appraiser, it seems unlikely that the going concern value of the
19 Company is presently less than the amounts owed to our Secured Creditors, particularly when one
20 considers that our revenues have increased significantly in 2009 and will do so again in 2010. On the
21 other hand, if the Company ceases to be a going-concern, its value in liquidation is likely to be a small
22 fraction of the 2008 appraised value and could well be inadequate to cover the Secured Creditors'
23 claims. It is in the best interests of QL2's unsecured creditors, its employees, and customers that the

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26 ¹ Blanket security interest filed under UCC Filing No. 2009-079-3428-0.

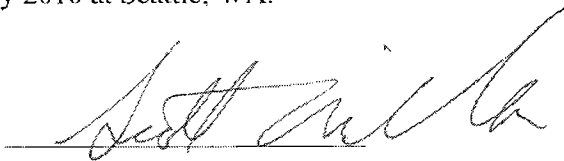
27 ² Blanket security interest filed under UCC 1 Filing No. 2009-323-2585-5.

28 ³ UCC 1 Filing No. 2007-099-6777-4.

1 Court grant it use of cash collateral on an interim basis in accordance with the budget (the "Budget")
2 attached hereto as **Exhibit B**.

3 25. No Unsecured Creditors Committee has yet been appointed in this case. Because of the
4 urgency of the circumstances surrounding QL2's applications for orders authorizing it to (i) pay pre-
5 petition payroll, benefits, and taxes, (ii) maintain certain of its prepetition bank accounts and cash
6 management system; and the potential for irreparable harm to QL2 should the relief requested be
7 delayed, (iii) pay identified critical vendors and (iv) use cash collateral; QL2 respectfully submits that
8 this motion should be granted without the requirement of further notice and hearing.
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10 EXECUTED this 12 day of January 2010 at Seattle, WA.
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14 Scott Milburn, Chief Operating Officer
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Employee	Gross Payroll Jan 1-11	Contractor	Contract Amt Jan 1-11			
Aldrich, Russell	6,363.64	Blue Gecko, IT Contractor	7,290.00			
Anderson, Trevor	1,723.49					
Baker, Gregory	1,531.25	Employ. Related Expenses	Jan1-11			
Bankston, Lauren	2,916.67	International Parking Mgt, Inc.	7,050.00	employee parking		
Bertrand, Jeffrey	2,916.66	Nationwide Trust Company, FSB	6,986.75	employee 401(k) contributions		
Bishop, Scott	1,060.61	WAHIT	22,883.44	employee health insurance		
Bozeman, Kerri	4,772.73	The Hartford - Priority Accounts	1,596.86	employee life & disability		
Bremer, Dale	1,988.64		38,517.05			
Brown, Ari	2,121.21					
Burgin, Joshua	2,837.12					
Campbell, Paul	3,977.27					
DeCamillo, Jodi	928.03					
Dechen, Christina	1,392.05					
Doyle, Nathan	1,643.94					
Elliott, Derrick	1,988.64					
Ghazal, Mark	3,977.27					
Hausler, Rosemary	4,454.55					
Hill, Justin	2,651.52					
Jacobs, Jeffrey	1,604.16					
Jantzen, David	3,181.82					
Jones, Timothy	2,518.94					
Judd, Daniel	1,590.91					
Khanna, Mahesh	24,095.67					
Klassen, Chris	2,863.64					
Knight, Franklin	3,309.09					
Koh, Seung	1,392.05					
Latimer, Peter	2,447.45					
Li, Sin Ming	1,909.09					
Martz, Alethea	2,253.79					
McCabe, James	2,651.52					
McFeely, David	2,625.00					
Meyer, Tara	1,458.34					
Milburn, Scott	5,303.03					
Neely, John	2,439.40					
Porter, Sarah	1,272.73					
Pusztai, Blake	1,590.91					
Reed, Susan	3,977.27					
Safford, Thomas	2,200.76					
Sandison, Shayne	1,378.79					
Saxer, Martin	3,049.24					
Shornal, Lyudmila	1,856.06					
Smith, Dale	3,181.82					
Stiglic, Angelique	1,447.73					
Taylor, Eric	1,531.25					
Thomassie, Sean	1,670.45					
Williams, Adam	2,020.45					
Zhao, Cen	1,458.34					
	137,524.97					

Ex. A

QL2 Software, Inc.

Budget - January - June 2010 (1/10/10)

	Jan-10	Feb-10	Mar-10	Apr-10	May-10	Jun-10
INCOME STATEMENT						
Bookings (Annualized)						
Renewals	316,089	442,524	505,742	493,479	690,870	789,566
New Bookings	300,000	500,000	600,000	600,000	600,000	600,000
Business Development	60,000	100,000	120,000	120,000	120,000	120,000
Total	676,089	1,042,524	1,225,742	1,213,479	1,410,870	1,509,566
Revenue						
Revenue	1,377,830	1,267,848	1,425,189	1,229,294	1,298,830	1,674,582
Cost of Revenue	165,000	165,000	165,000	165,000	166,065	177,741
Gross Margin	1,212,830	1,102,848	1,260,189	1,064,294	1,132,765	1,496,841
	88%	87%	88%	87%	87%	89%
Operating Expense						
Sales and Marketing	128,452	140,719	165,134	174,999	180,789	206,789
General and Administrative	193,304	193,304	193,304	222,793	222,793	222,793
Research and Development	254,827	254,827	262,494	287,346	287,346	287,346
International	107,500	107,500	107,500	110,725	110,725	110,725
Re-org Payments	65,000	0	0	0	0	85,000
Subtotal	749,083	696,351	728,432	795,864	801,654	912,654
EBITDA	463,747	406,497	531,757	268,430	331,111	584,187
Beginning cash	0	(106,976)	264,143	259,595	359,653	359,907
Cash receipts from operations	807,107	1,232,469	888,884	1,060,922	967,973	920,086
Cash disbursements from operation	(849,083)	(861,351)	(893,432)	(960,864)	(967,719)	(1,005,395)
Re-org payments	(65,000)	0	0	0	0	(85,000)
Ending cash	(106,976)	264,143	259,595	359,653	359,907	189,598

Ex. B

QL2 Software, Inc.						
Vendor		Amount monthly unless otherwise noted	Notes			
Adhost Internet		9,000				
ADP Tax Services		500				
Anonymizer, Inc.		9,000	quarterly			
AT&T Mobility*		250				
Blue Gecko (IT consulting)		30,000				
Cascade Broadband, LLC		30,000				
Cashmere Valley Bank		1,107				
CDW Direct, LLC		200	depending on usage			
CISCO WEBEX LLC		105				
Cit Technology Fin Serv, Inc.		1,054				
Citrix Online		5,535	quarterly			
City of Seattle (B&O Tax)		8,000	quarterly			
City of Seattle - Pioneer Square		150	quarterly			
Datasite Northwest		270				
Dell Financial Services		11,400	quarterly			
Denali Financial Consulting		15,000				
Dept of Labor & Industries		3,000	quarterly			
Dept of Revenue - WA		10,000	quarterly	varies by WSST each qtr		
DHL Express (USA) Inc.		100		depending on usage		
FedEx		200		depending on usage		
First Insurance Funding Group		3,904				
Flex-Plan Services		2,500		charged automatically		
International Parking Management, Inc.		3,000				
Mark Rostron (IT consultant)		15,000				
Nationwide Trust Company, FSB		10,000	401k employee contributions			
NetApp Financial Solutions		4,211	charged automatically			
Network Computing Architects Inc.		2,000				
Occidental Mall		24,000				
Parker Staffing Services		20,000				
Qwest		1,500				
Qwest AZ		3,200				
Qwest KY		2,000				
Rocky Mountain Equipment Leasing, LLC		10,950				
salesforce.com		12,000	quarterly			
Seadrunar Recycling		35				
SkyTel		100				
Sound Web Solutions		1,000				
Speakeasy		130				
T-Mobile		60				
Tableau Software		20,000	quarterly			
The Hartford - Priority Accounts		2,000	varies			
Travelers		2,000				
WAHIT		25,000				
WAHIT-Cobra Dept.		3,000	varies			

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